

**Office of Chief Counsel
Internal Revenue Service
memorandum**

CC:PA:APJP:B02:GThomas
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date: September 13, 2005

to: Doug Rogers, HQ Program Manager, SE:S:E:EP:PI
(Office of Penalties and Interest)

attn: Robert H. Curran, Tax Analyst

from:  Ashton P. Trice, Chief, Administrative Provisions & Judicial Practice, Branch 2
(Procedure & Administration)

subject: Failure to File Penalty on Subsequent Assessments

This memorandum responds to your request for assistance by email dated July 18, 2005. This advice may not be used or cited as precedent.

ISSUES

1. How is the failure to file ("FTF") penalty under I.R.C. § 6651(a)(1) calculated when a taxpayer claimed and was paid a refund from timely payments or credits reflected on a late-filed return, but the Service later determines a deficiency with respect to the return?
2. When does the minimum penalty under I.R.C. § 6651 for the failure to file penalty apply?

CONCLUSION

1. The FTF penalty is calculated using the amount of tax required to be shown on the return reduced by the amount of tax which was paid on or before the payment due date and the amount of any credit against tax which could be claimed on the return. In this case, that amount is equal to the deficiency minus the refund. This amount is then multiplied by the number of months the return was late and the FTF penalty is 5 percent of that amount.
2. If a taxpayer has a balance due and fails to file a return within 60 days of the due date including extensions, the minimum penalty applies whenever the FTF penalty will be less than \$100 or 100 percent of the amount required to be shown as tax on the return. The minimum FTF penalty is imposed only if the taxpayer has a balance due

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after payments made on or before the original due date of the return or applicable credits are applied to the correct amount of tax due for the tax year.

FACTS

We reviewed two examples in IRM 20.1.2.3.1(4) to determine whether they are consistent with the calculation of the failure to file penalty under Code sections 6651(a)(1) and 6651(b)(1). Example (c) provides:

A 1998 return is filed four months late on July 21, 1999 claiming a \$400 refund. The return is subsequently audited and a deficiency of \$700 is assessed. Since the \$700 is, per IRC section 6651(a)(1), "an amount required to be shown as tax" on the return, the FTF penalty is calculated by multiplying 5% per month, times four months, times \$700 = \$140. (Note: for FTF purposes, the amount subject to the penalty, i.e., \$700, is not offset by the \$400 refund on the return as filed.)

IRM 20.1.2.3.1(4)(c) (07/31/2001).

Example (a) provides:

An individual taxpayer files the 1997 return on June 19, 1998 with a tax liability of \$700 paid in full with the return. Since the FTF and the 1/2% FTP penalty under IRC 6651(a)(2) apply at the same time, the 5% FTF penalty is reduced to four and one half percent (.045). The FTF penalty rate of .045 a month, times three months, times \$700 = \$94.50.

IRM 20.1.2.3.1(4)(a) (07/31/2001).

LAW AND ANALYSIS

1. Calculation of Penalty

Section 6651(a)(1) provides that in the case of the failure to file any return on the date prescribed for filing including extensions, unless such failure is due to reasonable cause and not willful neglect, there shall be added to the amount required to be shown as tax on such return 5 percent of the amount of such tax for the first month, plus 5 percent for each additional month or fraction thereof during which the failure continues, but not to exceed 25 percent in the aggregate.

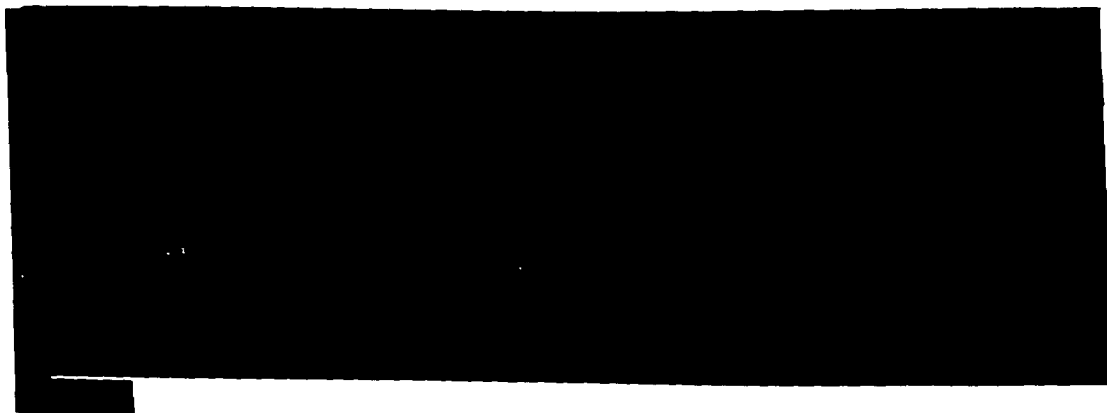
Section 6651(b)(1) provides that, for purposes of section 6651(a)(1), the amount of tax required to be shown on the return shall be reduced by the amount of any part of the tax which is paid on or before the date prescribed for payment of the tax and by the amount of any credit against the tax which may be claimed on the return.

The amount of tax required to be shown on the return for purposes of section 6651(a)(1) is initially determined regardless of any payments or credits. See Patronik-Holder v.

Commissioner, 100 T.C. 374, 379-381 (1993), acq., AOD-1994-03; Webb v. Commissioner, T.C. Memo. 1995-486. This amount is then reduced by any payments made on or before the original due date of the return. See Rev. Rul. 81-237 (the date prescribed for payment is the date fixed by section 6151(a) for the payment of tax without regard to any extension of time for paying the tax). Example (c) as shown above implies that the full amount of a deficiency on a late-filed return is always used to calculate the FTF penalty and payments or withholding credits refunded to a taxpayer are not treated as tax paid on or before the date prescribed for payment. Example (c) appears to be incorrect on its face.

The example does not provide whether the refund resulted from payments made on or before the date prescribed for payment such as withholding credits. If the refunded amount resulted from such payments, the FTF penalty in the example would be calculated by multiplying the product of 5 percent and 4 months by the amount of the deficiency that exceeds the refund to arrive at \$60. Because the return was not filed within 60 days of the date prescribed for filing the return in the example, the FTF penalty would be the lesser of \$100 or 100 percent of the amount of tax required to be shown on the return. In this case, the lesser of those two amounts is \$100 because 100 percent of the amount required to be shown on the return is at least \$700. See Minimum Amount Due, below.

Accordingly, we suggest that the example in the IRM be changed to read as follows:



2. Minimum Amount Due

The flush language in section 6651(a) provides that if the tax return is not filed within 60 days of the date prescribed for filing including extensions, unless such failure is due to reasonable cause and not willful neglect, the addition to tax under section 6651(a)(1) shall not be less than the lesser of \$100 or 100 percent of the amount required to be shown as tax on such return.

The minimum FTF penalty is calculated by reducing the amount of tax required to be shown on the return by any payments made on or before the original due date of the return or credits which may be claimed on the return under section 6651(b)(1). The

legislative history and the statutory language of section 6651 dictate that the minimum FTF penalty should be imposed only if the taxpayer has a balance due after such payments or credits are applied to the correct amount of tax due for the tax year. See Patronik-Holder v. Commissioner, 100 T.C. 374 (1993), acq., AOD-1994-03.

Pursuant to section 6651, example (a) shown above is incorrect. When a balance due return is filed more than 60 days after the due date, the addition to tax for failing to file the return should not be less than the lesser of \$100 or 100 percent of the amount required to be shown as tax on the return. Because 100 percent of the tax in example (a) is greater than \$100, the penalty in this example should be \$100. Therefore, we request that the IRM be updated to add the following to the end of example (a):

[REDACTED]

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call Glenn Thomas at (202) 622-7845 if you have any further questions.